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COMMENTS OF
THE ONTARIO GOVERNMENT
ON TRANSPORT CANADA'S

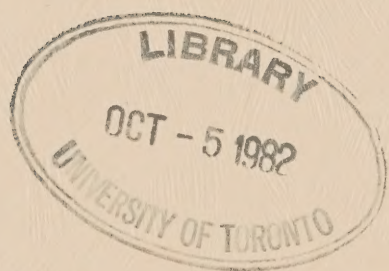
"PROPOSED DOMESTIC AIR CARRIER POLICY (UNIT TOLL SERVICES)"

NOVEMBER, 1981



Ontario

Ministry of
Transportation and
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COMMENTS OF THE ONTARIO GOVERNMENT ON TRANSPORT CANADA'S "PROPOSED
DOMESTIC AIR CARRIER POLICY (UNIT TOLL SERVICES)"

1. INTRODUCTION

The "Proposed Domestic Air Carrier Policy (Unit Toll Services)" circulated by Transport Canada for comments in August 1981, has been reviewed and the following comments have been prepared by the Ontario Ministry of Transportation and Communications.

The Ministry monitors the activities of the air service industry in Ontario to ensure that the Ontario public is adequately served. In addition, specific studies have been undertaken at the local air service level. The comments and recommendations contained in this response have been developed primarily from issues and activities that the Ministry has noted during its monitoring activities over the past several years.

2. SCOPE OF THE PROPOSED POLICY PAPER

Paragraph 2 of the policy paper states that one of the objects of the paper is "to describe and evaluate a proposal for a new policy defining the domestic unit toll roles of the National, Regional and Local commercial air carriers". This has been done in isolation of a number of related policy matters. For example, no consideration was given to transborder and international unit toll services, or to charter services offered by the charter-only operators or by the unit toll carriers themselves. In addition, the policy fails to take into consideration the possibility of a lessening of economic regulation as postulated in the earlier Transport Canada paper entitled "Economic Regulation and Competition in the Domestic Air Carrier Industry" and as recommended by the Economic Council of Canada in its report "Reforming Regulation, 1981". In fact, the underlying assumption throughout the paper appears to be that the present degree of regulation by the ATC will continue, at least for the foreseeable future. Such an approach can only result in the status quo being maintained.

The degree of economic regulation and competition permitted within the air carrier industry, the roles the various air carriers are permitted to undertake, both domestically and internationally, and the classes of services each type of air carrier may operate are inseparable issues and should be considered in unison. A sound air carrier policy can only be developed by looking at the industry as a whole rather than by attempting, independently, to develop policies for each sector of the industry.

3. ASSUMPTIONS

The policy paper recommends an evolutionary rather than a revolutionary development of the industry and this is certainly desirable. The Ontario Government also concurs that existing licences should continue to apply.

However, the kinds of restrictions the proposed policy places on the carriers, such as limiting the number of national and regional carriers and restricting the local carriers to non-jet equipment, impedes rather than stimulates such an evolutionary process.

Paragraphs 12, 19 and 31 of the policy paper state that the roles of the national (domestic) carriers and the local carriers have never been defined by government policy and that the regional carrier policy, as a result of a number of events, has become obsolete. With this in mind, it is difficult to understand why it was assumed in paragraph 39 that "abolishing the concept of roles for different groups of carriers at this time would be unduly disruptive". It seems that the carriers have been operating without defined roles for some time. Had this assumption not been made, a much wider range of policy options with greater scope to change carrier roles would have been open to discussion.

Paragraph 55 implies that a "real distinction between conventional unit toll services and specialized services catering to the leisure traveller" still exists. Yet in a discussion paper released in October 1980, which proposed the introduction of a Class 10 air carrier licence to regulate domestic ABC charter services, staff of the ATC stated "with the introduction of charter competitive fares by the scheduled carriers, there is now little distinction between scheduled passengers travelling at promotional fares and charter passengers". This latter statement better reflects the state of the industry. The major charter carriers and their services should have been considered as part of the policy.

The Ontario Government is pleased that the policy paper reaffirms, in paragraph 39, the Federal Government's responsibility to provide the necessary airport and air navigation facilities and services.

The Federal Government, however, has not assumed responsibility for municipal airports which handle a substantial amount of the local air service traffic. A number of provinces including Ontario have assumed a role in the development of local municipal and remote airports to support a minimum level of local services. Ontario has attempted to clarify the Federal/Provincial roles in this area but it appears that agreement on a policy acceptable to all provinces is still required.

With respect to subsidies for local air services, Ontario has been funding the norOntair system for ten years.

Also, regarding air navigation, we point out that a public system of aids to navigation to permit local carriers to operate under I.F.R. conditions does not exist yet in northern Ontario. Work is progressing to bring the system to an acceptable level and this must continue to be given a high priority.

4. CARRIER ROLES

The policy proposal defines carrier roles through a series of restrictions. For example, national carriers would not be permitted to operate aircraft of weight groups lighter than F except in exceptional circumstances, or to operate in northern Canada (north of 60°N latitude), and would be restricted to the present two, Air Canada and C.P. Air. Regional carriers would not be permitted to operate non-stop flights in excess of 800 great circle miles (1300 km) in southern Canada or to operate outside their respective regions, east or west of Winnipeg as the case may be. In addition, they would be restricted to the present four, three east of Winnipeg, and only one to the west. Finally, local carriers would be restricted to non-jet equipment except for all-cargo services, and would not be permitted to develop into regional carriers.

The third policy objective in paragraph 38 of the discussion paper is to "provide guidance to the Canadian Transport Commission without imposing a rigid structure on its consideration of whether a proposed service 'is and will be required by the present and future public convenience and necessity' ". While we agree that the proposed policy still permits the CTC some flexibility in its consideration of present and future public convenience and necessity, it places quite rigid conditions on whether or not the CTC might even consider a given carrier's application, public convenience and necessity notwithstanding. The proposed policy, therefore, is entirely too restrictive.

Ontario proposes a much less restrictive policy which defines the primary functions of each of the three types of carriers, but does not necessarily preclude them from offering other services.

Ontario's position with regard to carrier roles recognizes the need for the various groups of carriers to concentrate their activities in certain areas in order that a broad spectrum of services is provided to the public. This is achieved through identification of primary responsibilities for the carriers but without precluding them from providing other services.

Ontario would, therefore, define carrier roles as follows:

(a) Role of the National Carriers

The primary responsibility of the national carriers should be to provide service among major Canadian cities such as the national and provincial capitals, Montreal, Vancouver, Calgary, etc. Transborder and international routes should also be within their purview. However, this should not preclude them from offering services to other centres where high traffic volumes warrant such service. Also, this role could apply equally well in both northern and southern Canada, thereby allowing the nationals to offer scheduled services to the territorial capitals.

Ontario would not restrict the nationals to the use of large aircraft only (Group F and up) or limit them in number to the existing two carriers.

(b) Role of the Regional Carriers

The primary responsibility of the regional carriers should be to link regional centres and to provide a feeder system from regional to national centres. Their efforts should be concentrated within, but not necessarily restricted to their respective economic regions.

Within Canada, there are a number of distinctly different economic regions, e.g. the Atlantic provinces, Quebec, Ontario, the Prairies and the West Coast/Rocky Mountain region. If a carrier is based within the market it serves, it can be more attentive and responsive to the unique conditions that affect that market. The carrier's dependence for its own services would also become more localized. Local carriers would also benefit in that they could interface more effectively with the regional carrier within their respective regions.

Therefore, it is recommended that each region should be permitted to develop a regional carrier based within its own region if and when the opportunity presents itself. Each of these regional carriers should also be permitted to serve northern Canada and to operate short-haul transborder services. Canada's economic regions do not stop at the Canada/U.S.A. border and therefore, the regional carriers should be permitted to operate in the short/medium haul transborder markets.

The regional carriers should also be permitted to operate domestic, transborder and international charter-only services. If the nationals fail to adequately serve certain markets or if there is sufficient traffic demand to sustain additional competition, the regionals should also be given the flexibility to compete with the national carriers.

(c) Role of the Local Carriers

The primary role of the local carriers should be to link local centres and to provide a feeder system between local and regional or local and national centres. They should also be permitted to operate short-haul transborder services, both unit toll and charter. This should not preclude them from providing other services if and when regional carriers fail to meet market demands. In regions where a regional carrier does not exist, a successful local carrier should be permitted to evolve into a regional carrier. The policy proposal does not restrict local carriers to a given region and we agree with this aspect of the policy.

Local carriers should not be restricted to the use of non-jet equipment. Local carriers normally operate prop-driven aircraft and most are not in a financial position to purchase jet equipment. However, if a route has been developed by a local carrier to the point where jet equipment becomes appropriate and economically viable, the local carrier should not be restricted from expanding its operations. If the CTC denies the

local carrier the right to operate jet equipment in such a case, and also denies the regional or national carrier the right to operate the route because of the effect on the local carrier as suggested in paragraph 52, then it will be doing a disservice not only to the air carriers, but also to the public.

If further clarification of these roles is required, maps have been prepared describing existing national, regional and local air services operating in Ontario consistent with these definitions.

(d) Charter Services

The national carriers and, to a lesser degree, the regionals, are permitted to enter the charter-type market utilizing scheduled flights and they may also compete directly with the charter-only operators by adding ABC and similar Charter Flight Programs. Yet charter operators such as Wardair are denied the reciprocal right to compete in the unit toll market. We do not see the rationale or justice in continuing this one-sided policy. Over the long term, it is certain to have a serious negative impact on the financial viability of the charter-only operators. It is recommended that these charter operators, Wardair in particular, be permitted to compete with the scheduled carriers for unit toll services, provided the requirement to prove present and future public convenience and necessity is satisfied.

5. PUBLIC CONVENIENCE AND NECESSITY

The requirement to prove "present and future public convenience and necessity" would still remain as a criterion for determining what additional air services should be permitted. The extent to which new air services are licenced in Canada in the future will depend in large measure on the interpretation of this test by the Air Transport Committee. It would be worthwhile, therefore, for the government to provide some policy direction to the Committee in this regard.

An interesting discussion on the interpretation of "present and future public convenience and necessity" was included in the Air Transport Committee's Decision Number 6248 regarding STOL services in the Montreal/Toronto/Ottawa triangle.

The Committee noted that:

"The third element to the public convenience and necessity test consists of the expression "convenience and necessity". We sought to define this expression according to its ordinary meaning. After having resorted to dictionaries we found that both the word "convenience" and the word "necessity" refer to some sort of demand, the difference between the two being a matter of degree: "necessity" implies a stronger demand, one which if unsatisfied would make life extremely difficult if not impossible; "convenience" implies a milder demand, one which if unsatisfied would make life less tolerable or less pleasant but by no means impossible.

Given that the difference between "convenience" and "necessity" is one of degree, we have concluded that those words cannot co-exist and yet be given their ordinary meaning. Where the expression used, as in our case, is "convenience and necessity", the satisfaction of necessity automatically constitutes satisfaction of convenience, while satisfaction of convenience does not automatically constitute satisfaction of necessity; therefore, in such

an expression, the word "convenience", in its ordinary meaning, becomes meaningless as a criterion to be applied; the only criterion that matters is necessity.

Had the expression been "convenience or necessity", convenience would have been the only criterion that matters because once convenience would be established, the "public convenience or necessity" test would be satisfied; there would be no need to go one step further and prove necessity.

The corollary to our conclusion that the words "convenience" and "necessity" in the expression "public convenience and necessity" cannot be given their ordinary (i.e. dictionary) meaning, is that those words must be construed in terms of the context in which they appear, and in terms of the objects and purposes of the Aeronautics Act and the National Transportation Act, R.S.C. 1970 c. N-17."

The Committee went on to ask itself the following questions:

"Is it not reasonable to assume that when this legislation was enacted a greater degree of control was desirable, the air transport industry being at its very beginning? Is it not reasonable to assume that now that the air transport industry has matured and that Canada enjoys a wide network of commercial air services, a lesser degree of control is required? Is it not reasonable to assume that Parliament intended that there be room for flexibility in the exercise of control according to the evolution of the industry and to the circumstances of each case?"

We reasoned that the answer to each question should be affirmative, and recognized that subsection 16(4) (Aeronautics Act) is the means provided by Parliament for that flexibility. But we were still left with the problem of reconciling the words "convenience" and "necessity".

We have decided to resolve this problem by interpreting the expression "public convenience and necessity" in such a way as to remove the difference in degree which distinguishes "convenience" from "necessity". Thus, we concluded that the expression "public convenience and necessity" means public demand."

Clearly, the test of public convenience and necessity is open to interpretation by various Committees in the future. The current Committee's conclusion contained in Decision No. 6248, that less control is now required due to the mature state of the air service industry, should be confirmed. The Committee should be guided to place less emphasis on the proof of "necessity" in applications according to the interpretation in Decision 6248 which would lead to a greater degree of competition in the industry.

6. ECONOMIC REGULATION AND COMPETITION

Ontario's views on economic regulation and competition in the domestic air carrier industry were forwarded to Mr. W. M. McLeisch on July 23, 1981, in response to the report prepared on this subject by Transport Canada. Further clarification of these comments is now provided. As noted in Section 2 of this paper, we do not believe it is appropriate to separate the issue of economic regulation and competition from that of carrier roles.

Economic regulation of the airline industry encompasses five basic areas; market entry, market exit, mergers and acquisitions, prices, and licence or service restrictions. Ontario is of the opinion that various degrees of regulatory changes are warranted in each of these areas.

(a) Controls over Entry

Ontario recommends that more open entry should be permitted. In the case of applications to provide air service on routes where no other carrier currently operates, the ATC should place less emphasis on the requirement to prove present and future public convenience and necessity and more onus on opposing carriers to show why the service should not be introduced. This is particularly relevant in the case of local air services.

We do not, however, advocate an "open-skies" approach. Once a route has been licensed and a carrier is providing air service over the route, entry controls should be tightened with the onus returning to a new applicant to prove present and future public convenience and necessity. As the market matures and is able to sustain greater competition, entry controls should be gradually lessened resulting in a freer entry into the high density markets.

(b) Controls over Exit

Controls over exit from the market should be simplified. This could be achieved by establishing a simple notification requirement and a minimum elapsed time period unless a replacement carrier is

found earlier. In situations either where a new licence has been issued but the service has not been implemented within a certain time period, or where existing services have been discontinued for a given period of time, the licence should be cancelled.

(c) Controls over Mergers and Acquisitions

Mergers and acquisitions between smaller carriers could also be simplified particularly in cases where there will be no reduction in the quality or level of air service provided and/or where no opposition has been registered.

(d) Controls over Fares and Tariffs

In general, where competition exists, market forces are the most appropriate means of regulating air fares and tariffs. Therefore, airlines should be allowed to set air fares as they see fit, subject only to upward limits set by the regulator taking into account fuel and other cost increases. The setting of lower fares by an air carrier should be controlled by the regulator only to prevent air carriers from utilizing predatory pricing practices. Unlike the U.S. where there are a number of large air carriers competing, Canada's airline industry is dominated by Air Canada's sheer size and scope of operation. With this in mind, it is recognized that Air Canada's activities must be monitored to ensure the carrier does not undertake activities which would jeopardize the viability of the other carriers.

(e) Licence or Service Restrictions

Operational flexibility on the part of the carriers is required to permit the carriers to respond to changing market conditions. Fewer restrictions should be placed on licences once approved.

Through licensing restrictions, the ATC exercises a significant amount of control over terms and conditions of air service offered by the air carriers. These include restrictions on the type, size and number of aircraft operated, the frequency of air

services scheduled, the type of traffic carried, the number of intermediate stops between two points, etc. The original reasons for introducing such operational restrictions may no longer be valid and such operational decisions, therefore, are best left to the individual carriers.

7. SUMMARY AND RECOMMENDATIONS

Summary

In general, Transport Canada's proposed domestic air carrier policy is too restrictive. It will not allow sufficient flexibility either for the air carriers to adjust effectively to changes in market demands and economic conditions or for the Air Transport Committee in assessing air carrier's applications. Other than the proposed restrictions on equipment types for local and national carriers, the revised regional boundaries and the 800 mile limit for non-stop flights for regional carriers, the policy describes the status quo.

In particular, Ontario opposes those aspects of the policy which:

- (1) limit the national and regional carriers to the present two and four respectively;
- (2) define regional boundaries beyond which regional carriers may not operate;
- (3) inhibit the development of regional carriers in each of the economic regions of Canada;
- (4) restrict regional carriers to a maximum of 800 great circle miles for non-stop flights;
- (5) restrict local carriers to the operation of non-jet equipment and national carriers to the operation of aircraft in weight group F or higher; and,
- (6) prohibit Wardair and other charter-only carriers from entering the unit toll market.

In addition, the proposed domestic air carrier policy should not have been developed in isolation of the policies for charter, transborder and international services or the potential for a lessened regulatory environment.

Recommendations

Ontario recommends the following changes to the proposed Domestic Air Carrier Policy.

- (1) The policy should be developed in conjunction with policies on economic regulation and competition in the air carrier industry and international and transborder air carrier services.

- (2) The policy should be more flexible to better accommodate changes in market demands and economic conditions.
- (3) The policy should recognize the various economic regions within Canada and permit each region to develop its own regional carrier whose primary functions would be to serve that region. Such a policy, however, should not be designed to preclude the regionals from competing with one another or with the national carriers.
- (4) The definition of air carrier roles should be based on a set of primary responsibilities for each of the three carrier types but should not be so restrictive as to preclude the carriers from offering other services outside their primary roles.
- (5) National Air Carriers should:
 - (a) be permitted to expand beyond the present two carriers;
 - (b) be allowed to offer air services to the Arctic; and,
 - (c) not be restricted to the use of large aircraft only.
- (6) Regional Air Carriers should:
 - (a) be permitted to develop within each of the economic regions of Canada;
 - (b) be allowed to operate inter-regionally; and,
 - (c) not be restricted by a non-stop distance criterion.
- (7) Local Air Carriers should:
 - (a) be permitted to operate jet equipment; and,
 - (b) be permitted an opportunity to evolve into the regional carrier within their respective economic regions.
- (8) Charter-only operators such as Wardair should be permitted to enter unit toll markets if the test of public convenience and necessity conditions can be met.
- (9) Policy guidance should be given to the Air Transport Committee in the interpretation of "public convenience and necessity" to place more emphasis on the convenience aspect of this test rather than the necessity for air service. This should provide more open entry into unlicensed routes and competition on the higher density routes.

- (10) The existing regulatory procedures of the ATC should be reviewed with a view toward simplifying administrative procedures and reducing economic controls and service restrictions. More specifically, it is recommended that:
- (a) service-type restrictions placed on licences be eliminated;
 - (b) aircraft weight groups be simplified

e.g.	A - E	-	Group 1
	F & G	-	Group 2
	H (+)	-	Group 3;
 - (c) fewer controls be exercised over fares and tariffs with the regulator concentrating only on upper limits and predatory pricing practices;
 - (d) a regulatory philosophy be introduced that encourages competition among all carriers while, at the same time, recognizes that the sheer size and scope of Air Canada's operations would require some special considerations to protect the smaller carriers;
 - (e) exit procedures be simplified requiring notification of intent to exit and a minimum elapsed time before exit;
 - (f) licences be cancelled either where services are not implemented within a given time frame, or after services have been discontinued for a given period of time;
 - (g) merger and acquisition procedures be simplified where there is no reduction in service or no opposition registered; and,
 - (h) procedures concerning entry into routes not already serviced be simplified with more onus put on opposing carriers to show why the service should not be introduced and less on the applicant to prove public convenience and necessity.

